

**BILL ANALYSIS AND FISCAL IMPACT REPORT**  
**Rick Homans, Secretary, Taxation and Revenue Department**

**December 11, 2009**

**Bill:** 179321.2SA

**Sponsor:**

**Related Bills:**

**Short Title:** PIT Simplification

**Description:** The proposed legislation allows TRD to base look-up tables on Tax Table Income, incorporating in the look-up tables the standard deduction, personal exemption, the low- and middle-income exemption and tax rates; defines “Tax Table Income” to be adjusted gross income (AGI) plus adjustments and less exemptions and deductions except the standard deduction, personal exemptions and the low- and middle-income exemption; bases the phase-out of the low- and middle-income exemption on Tax Table Income rather than AGI; “decouples” the regular standard deduction and personal exemption amounts from the federal amounts (at their 2010 levels); “decouples” the personal exemption phase out from the federal amounts; simplifies the definition of “Modified Gross Income” and correspondingly adjusts LICTR; adds indexation of tax brackets, LICTR, and the low- and middle-income exemption for inflation; and updates the Income Tax Act, removing obsolete language and clarifying definitions and rules.

**Effective Date:** Tax years beginning on or after January 1, 2010

Estimated Revenue Impact*						R or NR**	Fund(s) Affected
FY2010	FY2011	FY2012	FY2013	FY2014	FY 10-14		
989	1,775	1,573	1,613	1,036	6,986	R	General Fund

\* In thousands of dollars. Parentheses ( ) indicate a revenue loss. \*\* Recurring (R) or Non-Recurring (NR).

**Policy Issues:** The bill would simplify the personal income tax, reducing the time taxpayers devote to record keeping, tax return preparation, return filing, and out-of-pocket payments to return preparers. The bill would also increase the fairness of the income tax, primarily by indexing the provisions of current law that are not currently indexed (rate brackets, the low- and middle-income exemption, and LICTR).

**Technical Issues:**

**Administrative Impact:** The income tax forms and instructions would need to be revised, and computer systems updated.

**Effect of Proposal:** Most taxpayers will be able to determine their income tax from the look-up tables using only their filing status, number of personal exemptions, and federal AGI. Itemizers will deduct the excess of their federal itemized deductions over the standard deduction, and the extra standard deductions for the elderly and blind will be preserved.

For taxpayers eligible for refundable rebates or credits, the computation of modified gross income will be much easier and require less record keeping.

The simplification achieved by the proposal is illustrated by the tax forms on pages 6 and 7.

The proposal would make the personal income tax fairer over time because it would be indexed for inflation. Currently, rate brackets, the low- and middle-income exemption, and LICTR lose value over time due to inflation, effectively imposing a tax increase due to inflation. Indexing of these amounts

would begin in 2011, using 2010 as the base year for indexing and an inflation adjustment factor of the percentage change in the Consumer Price Index (CPI) less 1% (“CPI - 1”). The CPI overstates the effect of inflation on taxpayers’ purchasing power because it does not take into account their ability to change purchasing patterns to mitigate the effect of price increases; using an inflation adjustment factor of CPI less 1% adjusts for this behavioral change and ensures that the revenue cost of indexing will be no greater than it is under current law.

Decoupling from the federal standard deduction and personal exemption amounts provides greater flexibility in designing New Mexico family- and child-related tax benefits. Decoupling from the federal standard deduction would also enable the State to make explicit decisions regarding whether to adopt (and therefore incur revenue losses associated with) special federal standard deductions. The personal exemption and standard deduction amounts would be indexed using the inflation adjustment factor CPI-1.

**Description - Detailed Discussion:** New authority would allow TRD to develop tax look-up tables that take into account the standard deduction, personal exemptions, and the low- and middle-income exemption (for taxpayers and dependents), so that taxpayers would not have to calculate these amounts.

Tax table income (used for the lookup tables) would be defined as: AGI plus NM additions to AGI less: (a) the excess of itemized deductions over the standard deduction, (b) NM subtractions (e.g., interest on NM state & local bonds, capital gains) and (c) NM uncompensated medical care deduction.

The low- and middle-income exemption is modified so that it phases out with “tax table income” rather than AGI.

Taxable income is determined in the same manner as “net income” under current law, except that the amount of the regular standard deduction and personal exemption, which are now coupled to the federal amounts, would be “decoupled” at their 2010 levels. The personal exemption phase out would also be “decoupled” from federal law.

The definition of “modified gross income” (MGI), which is used to determine eligibility for refundable rebates and credits (including LICTR), is amended so that MGI is simply federal adjusted gross income (AGI) plus social security and railroad retirement benefits excluded from AGI. So that very low- income taxpayers would not be adversely affected by the change in the definition of MGI, LICTR is modified such that the credit amount is constant below \$4,500 of income (the income level at which LICTR begins to phase out under current law).

The allowance of a LICTR exemption for children who are not dependents because the taxpayer does not meet the support test due to public assistance is repealed because it is no longer needed due to changes in the federal definition of a dependent child.

The standard deduction, personal exemption, tax brackets, low- and middle-income exemption, and LICTR would be adjusted for inflation beginning in 2011, using an inflation adjustment factor of CPI-1%.

“Net income” is no longer used to define taxable income, requiring some conforming changes in several sections of the Income Tax Act.

The special tax rate calculation for lump-sum amounts is repealed.

A new section is added to the Tax Administration Act that describes general rules for inflation indexing of the dollar value of an amount used to specify a tax, credit, rebate, or other provision.

Several definitions are added while some are deleted and some other obsolete language (e.g., concerning pre-1991 net operating losses) is removed.

See the “Section-by-Section Description” attached to this review.

### **Background Information:**

Taxable (“net”) income is computed under current law as follows:

Start with federal AGI

+ NM additions (e.g., interest on federally tax-exempt bonds)

- Federal standard or itemized deductions

- Federal personal exemption amount

- NM low- and middle-income exemption

- NM subtractions (e.g., interest on NM state and local bonds, capital gains)

- NM uncompensated medical care deduction

= NM taxable income

Tax liability is then computed at graduated rates that range from 1.7% to 4.9%.

Tax credits and rebates are then computed and subtracted from tax liability. Most credits are nonrefundable. Refundable rebates and credits (except the Working Families Tax Credit) are based on “Modified Gross Income” (MGI).

Withholding and estimated payments are applied.

Taxpayers compute their tax due or refund.

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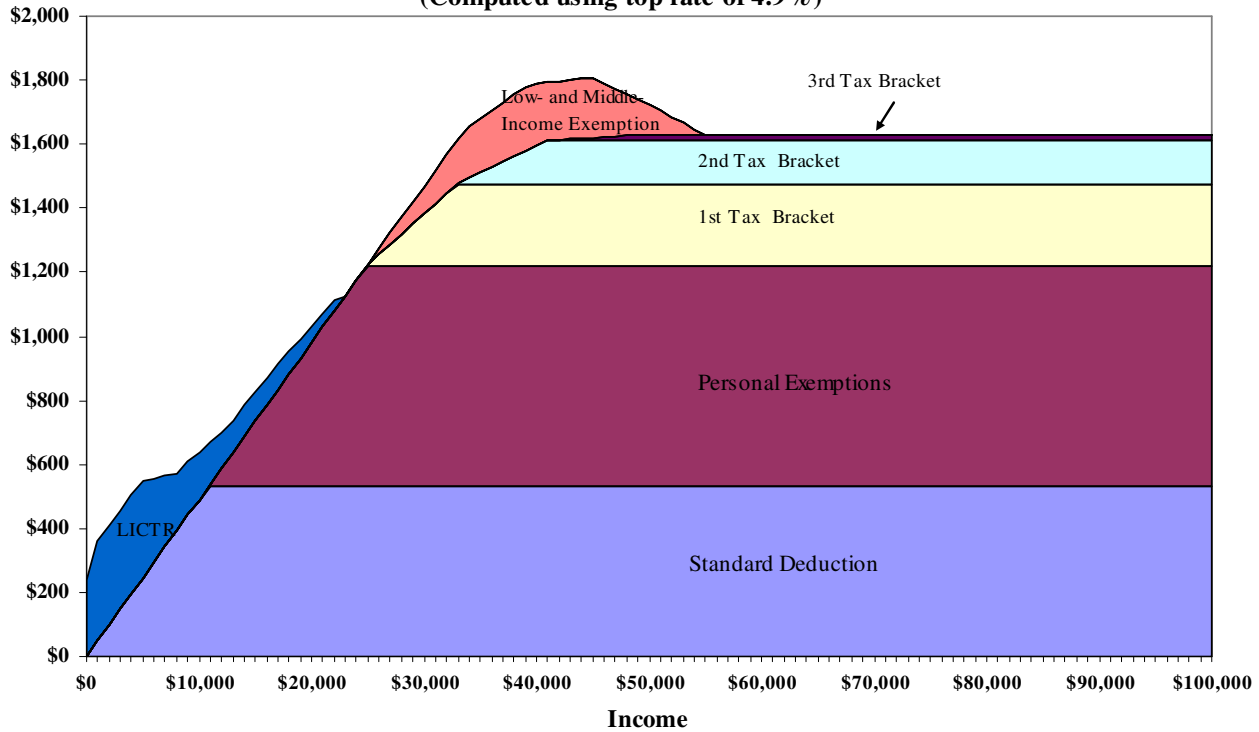
Progressivity is achieved primarily through certain family- and child-related tax benefits:

- Standard deduction
- Personal exemptions
- NM low- and middle-income exemption
- Graduated rates
- LICTR

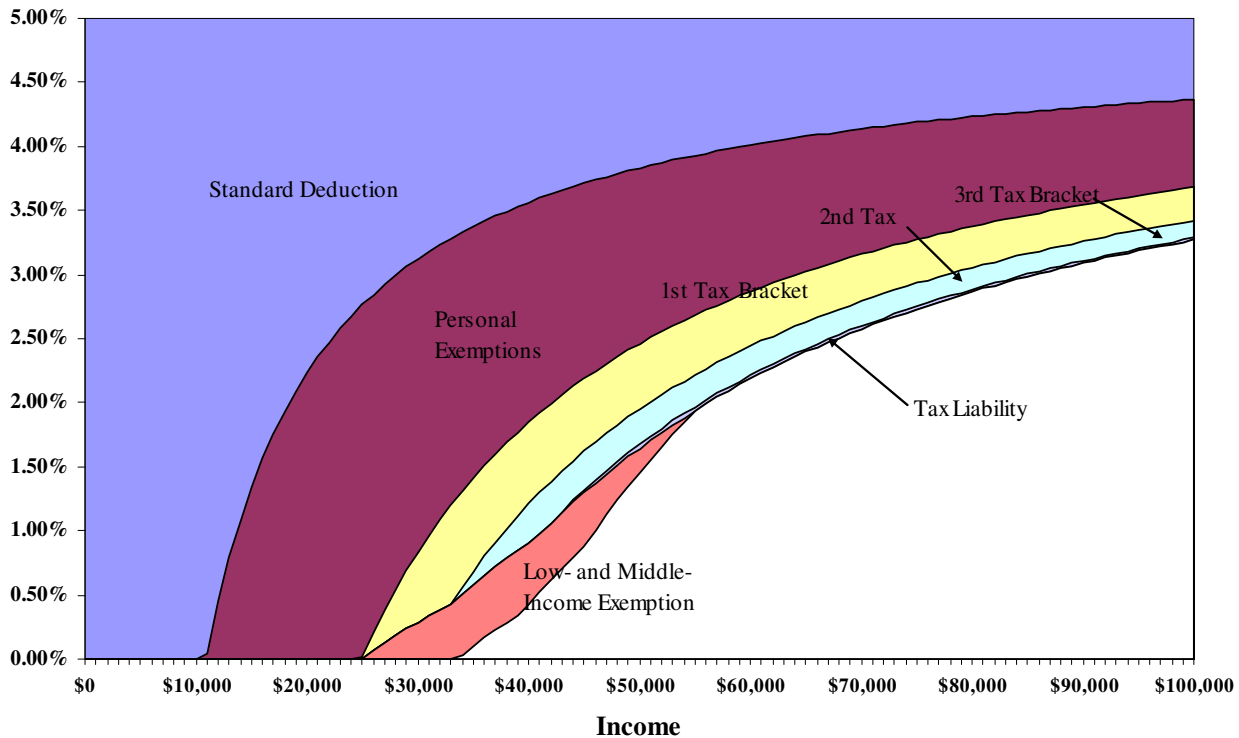
The following three graphs illustrate how these family- and child-related tax benefits contribute to progressivity. The first graph shows the dollar value of each of these benefits for a family of four at income levels up to \$100,000 (the computations are made using the top rate of 4.9%). The second and third graphs show these dollar amounts expressed as a percentage of income.

The Working Families Tax Credit also adds to progressivity. This credit is 10% of the federal EITC amount, and is only available to families with earned income.

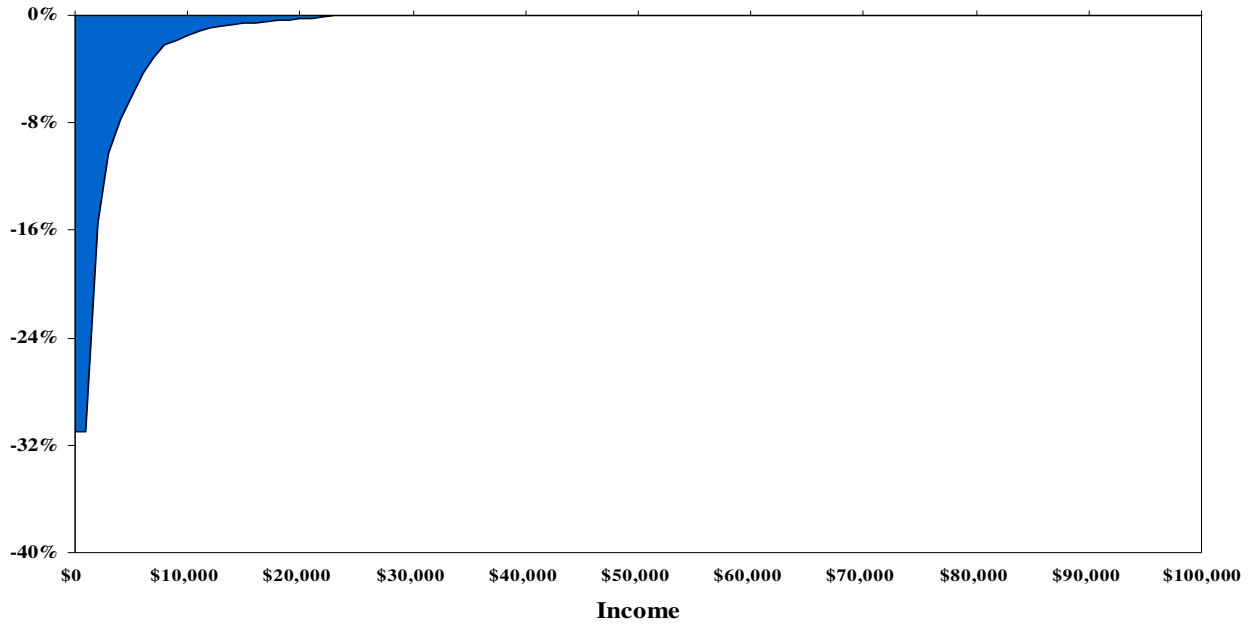
**Income Tax Benefits of Family and Child Related Tax Provisions  
for a Married Couple with Two Children  
(Computed using top rate of 4.9%)**



**Income Taxes as a Percentage of Income for a Married Couple with Two Children  
(Computed using top rate of 4.9%)**



**Low Income Comprehensive Tax Rebate (LICTR) as a Percentage of Income for a  
Married Couple with Two Children**



**2008 PIT-1 NEW MEXICO PERSONAL INCOME TAX**

For the year January 1 - December 31, 2008,

or other fiscal year beginning \_\_\_\_\_, ending \_\_\_\_\_.

If amending use Form 2008 PIT-X.

2008 PIT-1, PAGE 1  
39 BARCODE☐ Check this box if address is new or changed.

Print your name (first, middle, last)

Print your spouse's name (first, middle, last) Include spouse if married filing separately.

Mailing Address

City, State and ZIP Code

**1. SOCIAL SECURITY NUMBER**Residency status: complete  
for each taxpayer. Enter  
"R" if RESIDENT;  
"N" if NON-RESIDENT;  
"F" if FIRST-YEAR RES.;  
"P" if PART-YEAR RES..Check if taxpayer or spouse  
named on the return is deceased.  
Enter date of death.If a deceased taxpayer's refund must be made payable to a person other than the taxpayer or spouse  
named on the return, enter the name and SSN of that person. - You must also attach RPD-41083.2. ☐ ☐ **EXEMPTIONS** - Number of Qualified Exemptions.  
If you are a dependent of another taxpayer, enter 00.3. ☐ **EXTENSION OF TIME TO FILE** - Mark the box if  
you have a federal or state extension, and enter  
extension date.

\_\_\_\_/\_\_\_\_/\_\_\_\_

4. ☐ Check this box if federal Form(s)  
8886, *Reportable Transaction  
Disclosure Statement*, is required  
to be attached.**5. FILING STATUS - Check only one box below.**

- ☐ (1) Single
- ☐ (2) Married filing jointly
- ☐ (3) Married filing separately (Enter spouse's social security number above)
- ☐ (4) Head of household (Enter name of person qualifying you as head of household  
if that person is not counted as a qualified exemption on your federal return.)
- ☐ (5) Qualifying widow(er) with dependent child

**6. DEPENDENTS: As listed on your federal return**

(Report additional dependents on Schedule PIT-S)

First name	Last name	Dependent's SSN	Date of birth (MM/DD/CCYY)
			/ /
			/ /
			/ /
			/ /
			/ /

7. **FEDERAL ADJUSTED GROSS INCOME** .....  
(From line 38 of federal Form 1040, line 22 of Form 1040A or line 4 of Form 1040EZ)8. Additions to federal income (From line 4 of PIT-ADJ; **attach PIT-ADJ**)..... +~~9. Federal standard or itemized deduction amount (From line 40 of federal Form 1040, line 24 of Form  
1040A or line 8 of Form 1040EZ) .....~~~~9a. Check here if you itemized .....~~~~9b. Check here if you checked box 20a on federal Form 1040, or box 22a on federal Form 1040A .....~~~~10. Federal exemption amount (From line 42 of federal Form 1040, line 26 of Form 1040A, or  
leave blank if you filed Form 1040EZ) .....~~~~11. New Mexico low- and middle-income tax exemption (See PIT-1 instructions) .....~~12. Deductions/Exemptions from federal income (Line 20 of PIT-ADJ; **attach PIT-ADJ**)..... -~~13. Medical care expense deduction (See PIT-1 instructions) .....~~~~13a. Unreimbursed and uncompensated medical care expenses .....~~  
(You must complete both lines 13 and 13a or the deduction will be denied)14. **NEW MEXICO TAX TABLE INCOME** (Add lines 7 and 8, then subtract lines 9, 10, 11, 12 and 13)..... =

15. Tax on amount on line 14 ..... 15

If from the Look up Tables, enter "L". If from line 15 of PIT-B, enter "B" ☐~~16. Additional amount for tax on lump-sum distributions (See PIT-1 instructions) .....~~ +17. Credit for taxes paid to another state. You must have been a New Mexico resident during  
all or part of the year. (See PIT-1 instructions. **Include a copy of other state's return.**)..... -18. Non-refundable credits from Schedule PIT-CR (Line 16 of PIT-CR; **attach PIT-CR**)..... -19. **NET NEW MEXICO INCOME TAX** (Add lines 15 and 16, then subtract lines 17 and 18)..... =  
(Cannot be less than zero.)

Continue on the next page.

# 2008 PIT-RC NEW MEXICO REBATE AND CREDIT SCHEDULE

2008 PIT-RC, PAGE 1  
BARCODE

This schedule may be used by individuals who qualify for one or more refundable rebates and credits offered by New Mexico. Include Schedule PIT-RC with your Personal Income Tax Return, Form PIT-1.

Print your name (first, middle, last)

YOUR SOCIAL SECURITY NUMBER

**SECTION I: QUALIFICATIONS FOR REBATES AND CREDITS REPORTED IN SECTIONS II THROUGH V.** Complete Section I to claim the following rebates and credits in Sections II through V. To claim any refundable tax credits in Section VI, you do not need to complete Section I.

Persons with Modified Gross Income of:

**\$16,000 or less who are age 65 or older** may qualify for the **Property Tax Rebate**.

**\$27,248 or less** may qualify for the **New Mexico Child Day Care Credit**.

**\$22,000 or less** may qualify for the **Low Income Comprehensive Tax Rebate**.

**\$24,000 or less** who live in **Los Alamos County ONLY** may qualify for a **Low Income Property Tax Rebate**.

READ REBATE AND CREDIT SCHEDULE INSTRUCTIONS FOR COMPLETE ELIGIBILITY REQUIREMENTS.

- A. Were you a resident of New Mexico during any portion of the tax year? YES ☐ NO ☐
- B. Were you physically present in New Mexico for at least six months in 2008? YES ☐ NO ☐
- C. Were you a dependent of another taxpayer for income tax purposes in 2008? YES ☐ NO ☐

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## INMATE OF PUBLIC INSTITUTION

Check the appropriate box(es) if:

☐ TAXPAYER or ☐ SPOUSE  
was an inmate of a public institution in 2008  
for a period of more than six months.

## CALCULATE ALLOWABLE HOUSEHOLD MEMBERS AND EXTRA EXEMPTIONS

1. Number of exemptions from line 2 of Form PIT-1 ..... 1
2. a. Enter number of household members who DO NOT qualify. If all exemptions qualify, leave blank.  
(See PIT-RC instructions) ..... 2a -
- b. Subtract 2a from 1. Number of allowable household members ..... 2b =
- c. Extra Exemption: Check box if you are blind : ☒  
(If Married Filing Jointly) if your spouse is blind: ☒ Add the number of boxes checked. Enter here ..... 2c +
- d. Add lines 2b and 2c ..... 2d =
- e. If you are 65 or older enter "2" ..... 2e +
- f. If Married Filing Jointly and your spouse is 65 or older enter "2" ..... 2f +
- g. Add lines 2d, 2e and 2f ..... 2g =
- h. If you checked filing status (3) Married Filing Separately on your Form PIT-1, enter the number  
of exemptions your spouse claimed on line 2g of his or her PIT-RC if any ..... 2h +
3. Add lines 2g and 2h. Enter here and on line 13a on page 2 of this form ..... 3 =

**CALCULATE MODIFIED GROSS INCOME** - Modified Gross Income, generally, is all income of the taxpayer and household members, both taxable and nontaxable, and undiminished by losses. See instructions for certain types of income that do not have to be included in modified gross income.

**NOTE:** If Married Filing Separately, be sure to include spouse's income.

4. [Federal adjusted gross income] ..... 4 00
5. Social Security benefits, pensions, annuities and Railroad Retirement [Benefits not included in AGI] ..... + 5 00
6. Additions to federal income (From line 4 of PIT-ADJ; attach PIT-ADJ ) ..... + 6 00
7. Unemployment and Workers' Compensation benefits ..... + 7 00
8. Public assistance, TANF, welfare benefits and Supplemental Security Income (SSI) ..... + 8 00
9. Net profit from business, farm or rentals. If a loss, enter zero. Do not enter a negative number. .... + 9 00
10. Capital gains undiminished by capital losses ..... + 10 00
11. Gifts of cash or marketable tangible items received. (Must be given a reasonable value.) ..... + 11 00
12. All other income such as interest, dividends, gambling winnings, insurance settlements, scholarships, grants, VA benefits, trust income and inheritance, alimony and child support ..... + 12 00
12. Modified Gross Income (Add lines 4 through 11) Enter total on line 12 and on line 13 of page 2.  
(Must equal or exceed Federal Adjusted Gross Income from line 7 of Form PIT-1.) ..... = 12 00

## Section-by-Section Description

Section 1 (page 1, line 17 to page 3, line 3). Adds a new section (INDEXING AMOUNTS FOR INFLATION) to the Tax Administration Act (TAA) that describes general rules for inflation indexing of the dollar value of an amount used to specify a tax, credit, rebate, or other provision. Inflation indexing factors are based on changes in the consumer price index (CPI). After adjustment by the inflation indexing factor, amounts would be rounded according to their size; for example, amounts under \$500 would be rounded to the nearest \$1, amounts between \$500 and \$5,000 would be rounded to the nearest \$5, etc.

Note that this new section of the TAA does not result in inflation indexing of any amount in any current statute; it only provides the rules by which inflation indexing is computed if a tax, credit, or other statute provides for inflation indexing under this section.

Section 2 (pages 3, line 4 to page 13, line 24). This section amends Section 7-2-2, DEFINITIONS, of the Income Tax Act. There are four categories of changes to definitions: (1) changes related to describing how “taxable income” is computed; (2) the change in the definition of “modified gross income”; (3) new and deleted definitions; and (4) cleanup of existing definitions.

(1) Changes related to describing how “taxable income” is computed. These changes clarify the computation of taxable income by explicitly listing the adjustments (exemptions and deductions) from tax table income to New Mexico taxable income.

(2) The change in the definition of “modified gross income”. The new definition makes “modified gross income” the sum of federal adjusted gross income (AGI) and social security and railroad retirement benefits not included in AGI.

(3) New and deleted definitions. The definition of “dependent” is added (it had appeared elsewhere in the Income Tax Act), as are the definitions of “personal exemption” and “first year resident”. The concept of “net income” is not needed in the new computation of taxable income, so its definition is deleted. Likewise, the definition of “lump-sum amount” is deleted because under current rates there is no need for a separate computation of the tax on lump-sum amounts. A new definition is added for “tax table income”, and due to decoupling from federal law, definitions are added for “itemized deduction” and “personal exemption”.

(4) Cleanup of existing definitions. Several definitions are amended to conform with other changes or with current standards for statutory language, and to bring all the definitions related to “filing status” together.

Section 3 (page 13, line 25 to page 14, line 9). Makes conforming and cleanup changes to Section 7-2-3, IMPOSITION AND LEVY OF TAX.

Section 4 (page 14, line 10 to page 15, line 20). Adds a new section (7-2-3.1, ADDITIONS TO BASE INCOME) to the Income Tax Act, as part of the changes related to describing how tax table income is computed.

Section 5 (page 15, line 21 to page 17, line 12). Amends Section 7-2-4 (EXEMPTIONS) as part of the changes related to describing how taxable income is computed.

Section 6 (page 17, line 13 to page 19, line 18). Makes conforming and cleanup changes to Section 7-2-5.2, EXEMPTION—INCOME OF PERSONS SIXTY-FIVE AND OLDER OR BLIND.



Section 7 (page 19, line 19 to page 20, line 10). Makes cleanup changes to Section 7-2-5.5, EXEMPTION—EARNINGS BY INDIANS, THEIR INDIAN SPOUSES AND INDIAN DEPENDENTS ON INDIAN LANDS.

Section 8 (page 20, lines 11 to 23). Makes cleanup changes to Section 7-2-5.6, EXEMPTION—MEDICAL CARE SAVINGS ACCOUNTS.

Section 9 (page 20, line 24 to page 21, line 6). Makes cleanup changes to Section 7-2-5.7, EXEMPTION—INCOME OF INDIVIDUALS ONE HUNDRED YEARS OF AGE OR OLDER.

Section 10 (page 21, line 7 to page 23, line 14). Makes conforming and cleanup changes to Section 7-2-5.9, EXEMPTION—UNREIMBURSED OR UNCOMPENSATED MEDICAL CARE EXPENSES OF INDIVIDUALS SIXTY-FIVE YEARS OF AGE OR OLDER.

Section 11 (page 23, lines 15 to 22). Makes conforming changes to Section 7-2-5.10, EXEMPTION—NEW MEXICO NATIONAL GUARD MEMBER PREMIUMS PAID FOR GROUP LIFE INSURANCE.

Section 12 (page 23, line 22 to page 24, line 5). Makes cleanup changes to Section 7-2-5.11, EXEMPTION—ARMED FORCES SALARIES.

Section 13 (page 24, line 6 to page 26, line 7). Amends Section 7-2-7, INDIVIDUAL INCOME TAX RATES, by repealing the special computation of tax on lump-sum amounts and specifies indexing of tax brackets.

Section 14 (page 26, lines 8 to 23). Amends Section 7-2-7.1, TAX TABLES, to extend the authority of the Secretary of Taxation and Revenue to require the use of tables for the computation of tax. Also makes conforming changes.

Section 15 (page 26, line 24 to page 29, line 19). Makes conforming changes to Section 7-2-9, TAX COMPUTATION – ALTERNATIVE METHOD.

Section 16 (page 29, line 20 to page 32, line 23). Makes conforming and cleanup changes to Section 7-2-11, TAX CREDIT—INCOME ALLOCATION AND APPORTIONMENT.

Section 17 (page 32, line 24 to page 34, line 9). Amends Section 7-2-12, TAXPAYER RETURNS—PAYMENT OF TAX by a paragraph describing the requirement that taxpayers use the same filing status for New Mexico income tax purposes that they use (or would have used, if they had filed) on their federal income tax return. Also makes cleanup changes.

Section 18 (page 34, lines 10 to 24). Makes a conforming change to Section 7-2-12.1, LIMITATION ON CLAIMING OF CREDITS AND TAX REBATES.

Section 19 (page 34, line 25 to page 35, line 19). Makes conforming and cleanup changes to Section 7-2-13, CREDIT FOR TAXES PAID OTHER STATES BY RESIDENT INDIVIDUALS.

Section 20 (page 35, line 20 to page 39, line 22). Makes deletes obsolete language from Section 7-2-14, LOW-INCOME COMPREHENSITIVE TAX REBATE, modifies the credit

amount for very low-income taxpayers, and specifies indexing of the low-income comprehensive tax rebate.

Section 21 (page 39, line 23 to page 40, line 15). Makes conforming and cleanup changes to Section 7-2-32, DEDUCTION—PAYMENTS INTO EDUCATION TRUST FUND.

Section 22 (page 40, line 16 to page 41, line 23). Makes a conforming change and deletes obsolete language from Section 7-2-34, DEDUCTION—NET CAPITAL GAIN INCOME.

Section 23 (page 41, line 24 to page 45, line 16). Makes conforming and cleanup changes to Section 7-2-35, DEDUCTION—UNREIMBURSED OR UNCOMPENSATED MEDICAL CARE EXPENSES.

Section 24 (page 45, line 17 to page 46, line 14). Makes conforming and cleanup changes to section 7-2-36, DEDUCTION—EXPENSES RELATED TO ORGAN DONATION.

Section 25 (page 46, line 15 to page 47, line 11). Adds a new section (7-2-37, DEDUCTION—ITEMIZED OR SPECIAL STANDARD DEDUCTIONS) to the Income Tax Act that provides for the deduction of an amount equal to federal itemized deductions in excess of the standard deduction (if itemized deductions exceed the standard deduction allowed under Section 7-2-38). If the taxpayer did not itemize deductions on their federal return, the section provides for the deduction of the amount of the taxpayer's extra federal standard deduction for the elderly and blind. For a dependent taxpayer, the deduction is the amount they are allowed as a standard or itemized deduction on their federal return.

Section 26 (page 47, line 12 to page 48, line 7). Adds a new section (7-2-38, DEDUCTION—STANDARD DEDUCTION) to the Income Tax Act that sets standard deduction amounts equal to the 2010 federal standard deduction amounts and stipulates indexing standard deduction amounts pursuant to the Tax Administration Act beginning in 2011.

Section 27 (page 48, line 8 to page 49, line 16). Adds a new section (7-2-39, DEDUCTION—PERSONAL EXEMPTION AMOUNT) to the Income Tax Act that sets the per exemption amount equal to the 2010 federal personal exemption amount, specifies phase out of the personal exemption amount based upon adjusted gross income, and stipulates indexing the per exemption and threshold amounts pursuant to the Tax Administration Act beginning in 2011.

Section 28 (page 49, line 17 to page 52, line 4). Adds a new section (7-2-41, DEDUCTION—ADDITIONAL PERSONAL EXEMPTION AMOUNT FOR LOW- AND MIDDLE-INCOME TAXPAYERS) to the Income Tax Act. This section replaces section 7-2-5.8 and amends it to base the phase out on "tax table income".

Section 29 (page 52, lines 5 to 15). Makes conforming changes to Section 7-4-3 (ALLOCATION AND APPORTIONMENT OF INCOME IN GENERAL).

Section 30 (page 52, lines 16 to 17). Repeals Section 7-2-5.8, EXEMPTION FOR LOW- AND MIDDLE-INCOME TAXPAYERS.

Section 31 (page 52, lines 18 to 20). Makes the provisions of the bill applicable to taxable years beginning on or after January 1, 2010.